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NORTHERN DISTRICT OF CALIFORNIA

No. 03-44829 TT
Chapter 7

Debtor.

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On March 22, 2004, the Court issued an order directing the attorney of record for the above-captioned debtor (the "Debtor"), David Smyth ("Smyth"), to show cause why he should not be sanctioned for asserting frivolous claims in the above-captioned case.¹ Hearings were held on the order to show cause on May 5 and July 7, 2004. At the conclusion of the July 7, 2004 hearing, the Court took the matter under submission. The Court now concludes that Smyth violated Rule 9011(b) of the Federal Rules of Bankruptcy Procedure ("Rule 9011") by signing and presenting papers containing frivolous claims and by presenting those claims for an improper purpose. The reasons for this conclusion are set forth below as is the sanction to be imposed.

¹As discussed below, the above-captioned case was originally filed as a chapter 13 case and was ordered converted to chapter 7 on May 5, 2004.

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SUMMARY OF FACTS

During 1996 to 1998, the Debtor borrowed a total of \$500,000 from the City of Oakland (the "City") pursuant to a program established by the federal government to encourage the establishment of businesses in economically depressed urban areas (the "EEC Program"). As security for his obligation to repay these loans, the Debtor executed deeds of trust on his residence and his warehouse (the "Real Property") and a UCC-1 on his business personal property (the "Personal Property").

The Debtor defaulted almost immediately on his loan obligations to the City.² In January 2001, the City filed a complaint against the Debtor in state court, among other things, seeking to take possession of the Personal Property. At the same time, the City commenced nonjudicial foreclosure proceedings on the Real Property. Since then, the Debtor has managed to prevent the City from foreclosing through a series of legal actions. A detailed account of the Debtor's and the City's loan and litigation history is set forth in a separate memorandum issued herewith (the "Adversary Proceeding Memorandum").

The Debtor's most recent effort to forestall foreclosure was by filing this chapter 13 case. On August 21, 2003, Smyth filed a petition commencing this case on behalf of the Debtor. At that time,

²The City has represented to the Court that the Debtor made only two payments on his loan obligations. The Debtor has admitted in papers filed either in this case or in the Debtor's adversary proceeding against the City (the "Adversary Proceeding") that the last payment he made to the City was in 1996.

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1 Smyth was familiar with the Debtor's litigation history, having
2 represented the Debtor in connection with his previous state court
3 action.

4 During the early months of the chapter 13 case, it appeared that
5 the Debtor had accepted the necessity of repaying the City. The
6 Debtor scheduled the City's claims as secured and undisputed
7 (although the amount of the claim scheduled was considerably less
8 than the City contends is due). The Debtor filed a chapter 13 plan
9 (the "Plan") stating that he would pay the City's claim by April 1,
10 2004 through a sale or refinance of the Real Property.³ In other
11 papers filed with the Court shortly before the Plan was confirmed,
12 the Debtor stated that he had already located a buyer for the Real
13 Property. The City did not object to the Plan, and the Plan was
14 confirmed.⁴

15
16 ³The Debtor scheduled only three creditors, all secured: i.e.,
17 the City, the Alameda County Tax Collector (the "Tax Collector"),
18 and the Bank of Oakland. The Plan proposed that the Debtor would
19 pay the trustee nominal amounts on a monthly basis, \$100 month for
20 the first year, then \$280 a month. Paragraph 2(b) provided that
21 the chapter 13 trustee (the "Trustee") would use these amounts to
22 pay the amount due to the Tax Collector. The Debtor was apparently
23 current with the Bank of Oakland (the "Bank"). Paragraph 4 of the
24 Plan stated that the Debtor would pay the Bank of Oakland \$900 per
25 month directly. The Plan stated that unsecured creditors would be
26 paid 100 percent. The provision dealing with the City's claim was
set forth on an attached page, to which paragraph 7 of the Plan
referred.

⁴Shortly after the Plan had been recommended for confirmation,
the Debtor filed the Adversary Proceeding. In the Adversary
Proceeding, the Debtor asserted claims against the City, in defense
of his obligation to repay the City's loans, that had been rejected
by both the federal district court and the state court in previous
litigation. The City filed a motion for sanctions in the Adversary
Proceeding which the Court has granted. The Court's conclusions

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After confirmation, the City filed proof of claim (the "City's Proof of Claim"), asserting a secured claim for \$983,146.51. On March 10, 2004, the Debtor filed an objection to the City's Proof of Claim (the "Claim Objection"). In the Claim Objection, Smyth asserted that confirmation of the Plan had caused the City to lose its security interest because the City's claim was not listed in paragraph 2(b) and was not expressly described as secured. He also asserted that the City had no right to be paid on an unsecured basis because the City's Proof of Claim asserted that its claim was secured, not unsecured. The Court's order to show cause was based on these contentions.⁵

DISCUSSION

A. LAW APPLICABLE TO RULE 9011 SANCTIONS

The Court's order to show cause advised Smyth that, if the Court concluded that sanctions were appropriate, it might base its sanctions on Rule 9011, 28 U.S.C. § 1927, or 11 U.S.C. § 105. After further consideration and research, the Court concludes that sanctions should be imposed only under Rule 9011.⁶

with respect to the City's motion and the sanctions to be imposed based on that filing are set forth in the Adversary Proceeding Memorandum.

⁵Smyth filed two amended objections to the City's Proof of Claim after the Court issued its order to show cause, adding additional bases for objecting to the City's claim. The Court declines to address these additional contentions since they were not made part of its order to show cause.

⁶Under Ninth Circuit law, the bankruptcy court may not issue sanctions under 28 U.S.C. § 1927 because it is not considered a "court of the United States" as required by that statute. In re

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Rule 9011(b) (1) provides that an attorney may be sanctioned for presenting papers to a court for any improper purpose, such as to harass or to cause unnecessary delay or needless increase in the cost of litigation. Rule 9011(b) (2) provides that an attorney may be sanctioned for signing and presenting a paper to the court containing frivolous claims, defenses, and legal contentions. Violations of either Rule 9011(b) (1) or (b) (2) are judged by an objective standard: i.e., what a reasonable attorney would have done. The Court need not find that the attorney acted with subjective bad faith. Bus. Guides, Inc. v. Chromatic Communications Enters., Inc., 892 F.2d 802, 809-12 (9th Cir. 1989), aff'd, 498 U.S. 533 (1991).

Rule 9011(c) permits a court to impose sanctions on its own initiative by issuing an order to show cause. The order to show cause must describe the conduct complained of, and the attorney must be given an opportunity to demonstrate that his conduct did not violate Rule 9011(b). The sanctions imposed must be limited to what is sufficient to deter repetition of comparable conduct by others similarly situated and may include nonmonetary sanctions. When imposing sanctions, the court should describe the conduct giving rise

Sandoval, 186 B.R. 490, 495 (Bankr. 9th Cir. 1995) (relying on In re Perroton, 958 F.2d 889 (9th Cir. 1992), which reached this conclusion in the context of another similar federal rule). The Court does have the power to sanction Smyth under 11 U.S.C. § 105. See In re Rainbow Magazine, Inc., 77 F.3d 278, 283-85 (9th Cir. 1996). However, to do so, it must find that Smyth acted in bad faith, judged by a subjective standard. See In re Mroz, 65 F.3d 1567, 1576 (11th Cir. 1995). By contrast, as discussed below, Rule 9011 sanctions are governed by an objective standard.

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1 to sanctions and explain its rationale for imposing them.

2 **B. BASIS FOR SANCTIONS**

3 The Court bases its conclusion that Smyth should be sanctioned
4 under Rule 9011(b)(1) and (2) on the two legal contentions made in
5 the Claim Objection. As discussed above, first, Smyth contended that
6 the City's secured claim could not be paid through the Plan because
7 the Plan did not provide for its payment as a secured claim. Second,
8 he contended that the City could not be paid through the Plan as an
9 unsecured creditor because the City did not file a proof of claim for
10 an unsecured claim, only a proof of claim for a secured claim. The
11 Court finds both contentions frivolous.

12 Smyth based his first contention, in part, on the fact that the
13 Plan does not expressly refer to the City's claim as secured.
14 However, there is no requirement that a plan specifically refer to a
15 claim as secured for the claim to be paid through the plan as a
16 secured claim. Only two things are required. The creditor must file
17 a timely proof of claim asserting secured status, and the plan must
18 provide for its payment. See 11 U.S.C. § 1327(c). Here, both
19 requirements were satisfied.

20 Smyth also contended that the Plan did not provide for payment
21 of the City's claim as a secured claim because the provision dealing
22 with the City's claim was not set forth in paragraph 2(b). This
23 contention is also frivolous. Paragraph 2(b) of the Court's form
24 plan is only designed for secured claims whose arrearages will be
25 paid by the chapter 13 trustee on a monthly basis from the debtor's
26 monthly plan payments. The Plan did not provide for any monthly

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1 payments to the City by the trustee. Instead, it provided that the
2 debtor would pay the City's claim directly from the sale or refinance
3 of the Real Property by April 1, 2004.⁷

4 Smyth did not assert in the Claim Objection that confirmation of
5 the Plan actually caused the City to lose its lien, only that it
6 could not be paid through the Plan. However, in papers filed in
7 connection with this order to show cause, Smyth did make this further
8 frivolous assertion. In support, he cited In re Harnish, 224 B.R. 91
9 (Bankr. Iowa 1998). The Harnish court noted split of authority on
10 this issue.

11 The Ninth Circuit has recently held to the contrary. See In re
12 Enewally, 368 F.3d 1165, 1173 (9th Cir. 2004) (plan provisions may not
13 provide relief that requires an adversary proceeding). However, at
14 the time the Claim Objection was filed, the highest authority in the
15 Ninth Circuit on this issue was In re Shook, 278 B.R. 815, 824
16 (Bankr. 9th Cir. 2002). In Shook, the Bankruptcy Appellate Panel held
17 that a chapter 13 plan could effectively avoid a lien provided the
18 creditor received clear notice that the plan would do so. Shook, 278
19 B.R. at 824.

20 Regardless of the lack of any higher authority at the time the
21 Claim Objection was filed, however, Smyth could not plausibly contend
22 that confirmation of the Plan resulted in the avoidance of the City's
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25 ⁷Similarly, the proposed treatment of the claim of another
26 secured creditor, the Bank of Oakland (the "Bank"), was not
included in paragraph 2(b). The Debtor apparently was current on
his payments to the Bank. Paragraph 4 of the Plan stated that the
Debtor would pay the Bank \$900 a month directly.

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1 liens. The Court is unaware of a single case in any jurisdiction
2 holding that a creditor who is scheduled as having an undisputed and
3 secured claim, which the plan states will be paid in full, and who
4 files a timely proof of claim asserting secured status loses its lien
5 when the plan is confirmed.⁸

6 Smyth's second contention is even more clearly frivolous. In
7 the Claim Objection, Smyth cited a case purportedly in support of his
8 contention: In re Avery, 272 B.R. 718 (Bankr. E.D. Cal. 2002).
9 However, the only relevant statement made in that case is that a
10 creditor may not be paid through a chapter 13 plan unless it files a
11 proof of claim. Avery, 272 B.R. at 723, n.5. In papers filed in
12 connection with the order to show cause, Smyth admitted that he had
13 no authority for his second contention.

14 While an attorney may not be sanctioned for making a creative
15 argument, the argument must be plausible. Smyth's contention is
16 ridiculous. A creditor must be able to rely on a proof of claim
17 asserting secured status to preserve its underlying monetary claim in
18 the event its security interest is avoided. Otherwise, it would have
19 to file multiple claims or plead in the alternative in every case on
20 the chance that a debtor might challenge its lien.

21 The Court also concludes that, judged objectively, Smyth made
22 these two arguments for an improper purpose. A reasonable attorney
23 would not have made these arguments. As a result, the Court
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26 ⁸Underscoring the frivolity of this contention, Smyth has
conceded that, when he drafted the Plan, he did not intend it to
have that effect.

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concludes that he also violated Rule 9011(b)(1). See Bus. Guides, Inc. v. Chromatic Communications Enters., Inc., 892 F.2d 802, 809-12 (9th Cir. 1989), *aff'd* 498 U.S. 533 (1991).

B. APPROPRIATE PENALTY

The only thing remaining is to determine an appropriate sanction to be imposed on Smyth for signing and presenting the Claim Objection. Rule 9011(c) directs the Court to impose the least severe sanction likely to accomplish the deterrence purpose of the rule. See Zambrano v. City of Tustin, 885 F.2d 1473, 1480 (9th Cir. 1989). In making this determination, the Court must necessarily consider any previous sanctions that have been imposed on Smyth for similar behavior and the extent to which they have had any deterrence effect.

The Court notes that Smyth has a lengthy history of disciplinary problems. As he has conceded in his papers, many years ago, he was the object of a malpractice judgment. Thereafter, over ten years ago, the three bankruptcy judges in the Oakland division, based on their observations of his incompetence and unprofessional conduct, advised Smyth that he would not be appointed to represent chapter 11 debtors.

Still more recently, in *In re Kellander*, Case No. 99-17645, Smyth was sanctioned \$6,000 for filing a frivolous motion to avoid a judgment lien for child support despite the statutory exclusion of such liens from avoidance. The sanction was imposed by the Honorable James Grube of the San Jose division, after the judge assigned to the case, the Honorable Randall Newsome, recused himself. Judge Grube also required Smyth to complete 40 hours of continuing legal

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1 education in the field of consumer bankruptcy law and legal ethics.⁹
2 Judge Grube's decision was affirmed by the Bankruptcy Appellate Panel
3 and by the Ninth Circuit. See In re Kellander, 2001 WL 599229 (9th
4 Cir.).

5 Clearly, Judge Grube's sanction was insufficient to deter
6 Smyth's continued unprofessional conduct. In response to the City's
7 motion for Rule 9011(b) sanctions in the Adversary Proceeding, the
8 Court has ordered that Smyth pay the City's attorneys' fees and costs
9 incurred in connection with that matter in the total amount of
10 \$10,671. However, the Court concludes that this does not constitute
11 a sufficient sanction for filing the Claim Objection.

12 Rule 9011(c) also permits the Court to impose nonmonetary
13 sanctions. See Doering v. Union County Bd. Of Chosen Freeholders,
14 857 F.2d 191, 194 (7th Cir. 1988) (enumerating possible types of
15 monetary sanctions). Judge Grube's continuing education sanction
16 appears to have done little good. Somethin more severe is therefore
17 required. Although the Court warned Smyth that it would consider
18 disbarment proceedings, it has concluded that the least severe
19 sanction requirement counsels for a six month suspension from
20 practice instead.

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25 ⁹Because Judge Grube's order was not published, a copy of the
26 order is attached hereto. The order provides a history of Smyth's
prior misconduct and vividly illustrates some of Smyth's
deficiencies.

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CONCLUSION

The Court concludes that Smyth violated Rule 9011(b) (1) and (2) by filing and presenting the Claim Objection to the Court. The Court is mindful of Smyth's history of disciplinary proceedings and the monetary sanction ordered herewith in connection with the Adversary Proceeding. Nevertheless, the Court concludes that an additional sanction is required to accomplish the rule's deterrence purpose. Therefore, the Court will suspend Smyth for six month suspension from practice in the bankruptcy courts of this district. The six month period will run from the effective date of the order imposing the sanctions. The bar will exclude those cases already filed in which Smyth has already appeared as attorney of record.

Dated: September 1, 2004

United States Bankruptcy Judge

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PROOF OF SERVICE

I, the undersigned, a regularly appointed and qualified clerk in the office of the United States Bankruptcy Court for the Northern District of California at Oakland, hereby certify:

That I, in the performance of my duties as such clerk, served a copy of the foregoing document by depositing it in the regular United States mail at Oakland, California, on the date shown below, in a sealed envelope bearing the lawful frank of the Bankruptcy Court, addressed as listed below.

I declare under penalty of perjury under the laws of the United States that the foregoing is true and correct.

Dated: September ___, 2004

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